

IN THE CHANCERY COURT OF THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY

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STATE OF TENNESSEE, ex rel.)
PAULA A. FLOWERS, Commissioner of)
Commerce and Insurance for the State)
of Tennessee,)

Petitioner,)

v.)

No. _____

UNIVERSAL CARE OF TENNESSEE,)
INC., a Tennessee for-profit health)
maintenance organization, UNIVERSAL)
CARE HEALTH SYSTEMS, INC., a)
California corporation, and UNIVERSAL)
CARE, INC., a California corporation,)

Respondents.)

**VERIFIED PETITION FOR APPOINTMENT OF RECEIVER
FOR PURPOSES OF LIQUIDATION AND INJUNCTION**

Petitioner, Paula A. Flowers, Commissioner of Commerce and Insurance for the State of Tennessee ("Commissioner" or "Department"), by her counsel, Paul G. Summers, Attorney General of the State of Tennessee states as follows:

I. NATURE THE ACTION

1. This action is brought by the Commissioner pursuant to the Insurers Rehabilitation and Liquidation Act, Tenn. Code Ann. §§ 56-9-101, *et seq.* (hereinafter the "Act"), and Tenn. Code Ann. § 56-32-217, seeking the appointment of a receiver for purposes of liquidation of UNIVERSAL CARE OF TENNESSEE, INC., ("Universal"). Universal Care of

liquidation of UNIVERSAL CARE OF TENNESSEE, INC., (“Universal”). Universal Care of Tennessee, Inc. is a for-profit corporation licensed to operate as a health maintenance organization (“HMO”) in the State of Tennessee. Pursuant to an Amended and Restated Contractor Risk Agreement (“CRA”), Universal contracted with the State as a managed care organization (“MCO”) to provide or arrange for health care services to be provided to certain eligible enrollees in Tennessee’s TennCare Program. Universal provided health care services to approximately 95,000 TennCare enrollees until June 1, 2003, at which time the CRA terminated.

Respondent Universal Care, Inc. (“UCI”), is named as a party because Universal has asserted it has entered into a contract with UCI for it to manage most of Universal’s operations. Although this contract has not been approved by Tennessee Department of Commerce and Insurance (“TDCI”), it is believed that management of Universal’s operations was indeed being performed by UCI, as of June 1, 2003. Accordingly, specific provisions of liquidation and related injunctions will require cooperation and acts by UCI. Respondent Universal Care Health Systems, Inc. (“UCHS”) is named as a party because it also entered into a contract with Universal to allegedly manage most of Universal’s operations, and specific provisions of liquidation and related injunctions require cooperation and acts by UCHS. The Commissioner also requests an injunction against suits and other acts that could interfere with the efforts of the receiver.

2. The Commissioner has reasonably determined that Universal is insolvent and/or in a condition which is hazardous, financially and otherwise, to its enrollees, providers, creditors and the public in general, as discussed further herein. The Commissioner has further determined, based upon Universal’s hazardous and worsening financial condition, as well as the termination

by the State of the CRA with Universal, that any attempts to rehabilitate Universal would substantially increase the risk of loss to enrollees, creditors and the public and/or would be futile.

II. JURISDICTION AND VENUE

3. This Court has subject matter jurisdiction of this action pursuant to Tenn. Code Ann. § 56-9-104, and venue of this action is properly in the Chancery Court of Davidson County pursuant to Tenn. Code Ann. § 56-9-104(e).

III. THE PARTIES

4. The Petitioner, Paula A. Flowers, is the duly appointed Commissioner of Commerce and Insurance for the State of Tennessee. Pursuant to Tenn. Code Ann. §§ 56-9-101, *et seq.*, the rehabilitation, liquidation or conservation of a domestic insurance company is to be conducted by the Commissioner after her appointment as receiver by the Court. Tenn. Code Ann. §§ 56-9-301, *et seq.* Pursuant to Tenn. Code Ann. § 56-32-217(a), any rehabilitation, liquidation or conservation of an HMO shall be deemed to be the rehabilitation, liquidation or conservation of an insurance company and shall be conducted under the supervision of the Commissioner, pursuant to Chapter 9 of Title 56 of the Tennessee Code Annotated.

5. Respondent Universal Care of Tennessee, Inc., is a for-profit corporation, incorporated in the State of Tennessee and holding a certificate of authority from the Commissioner to operate as a Tennessee domestic HMO, thereby becoming subject generally to the standards of Tenn. Code Ann. §§ 56-32-201, *et seq.* Universal had contracted with the State

of Tennessee's TennCare Bureau in the Department of Finance and Administration to provide health care benefits to persons enrolled in the State's TennCare program, until June 1, 2003, when the CRA terminated. Universal operated a TennCare health plan which served approximately 95,000 TennCare enrollees at the time of termination. Universal received 100% of its revenue from the CRA with the State. The President and CEO of Universal is Jay B. Davis. Universal's principal offices are shown on its annual reports to the Secretary of State as 1600 E. Hill Street, Signal Hill, California 90806-3682, and it may be served with process by delivering a copy of the summons and petition to John Hicks, 511 Union Street, Nashville, Tennessee 37219, Universal's registered agent for service of process.

6. Universal Care, Inc., ("UCI") is a California corporation licensed to operate as a "staff model health care service plan" in that state since 1985. It is owned 100% by Howard E. Davis, chairman of the Board of Universal and the father of Jay B. Davis, President and CEO of Universal and Executive Vice-President of UCHS, and Jeff Davis, CFO of Universal. UCI's principal offices are also located at 1600 E. Hill Street, Signal Hill, California 90806-3682, and it may be served with process by delivering a copy of the summons and petition to John Hicks, 511 Union Street, Nashville, Tennessee 37219, UCI's registered agent for service of process. Universal has asserted that UCI entered into a management contract with Universal, which has not been approved by TDCI, for the management and provision of most of the administrative services associated with the performance of Universal's TennCare contract. A copy of this contract, filed with TDCI by Universal on March 10, 2003, is attached hereto as Exhibit A and incorporated herein by this reference. It is believed that UCI has been providing most of the necessary administrative services to Universal, at least during 2003. Accordingly, it appears that

any liquidation of Universal cannot be carried out without the full cooperation of UCI and its agents, employees, officers and directors. As such, UCI is named and served as a party Respondent here so as to assist in obtaining its full cooperation.

7. Respondent Universal Care Health Systems, Inc., (“UCHS”) is a California for-profit corporation. Its Executive Vice President is Jay B. Davis, who is also President and CEO of Responsent Universal. UCHS’s principal offices are also located at 1600 E. Hill Street, Signal Hill, California 90806-3682, and it may be served with process by delivering a copy of the summons and petition to John Hicks, 511 Union Street, Nashville, Tennessee 37219, UCHS’s registered agent for service of process. In January 2001, UCHS also entered into a management contract with Universal, which was approved by TDCI, for the management and provision of most of the administrative services associated with the performance of Universal’s TennCare contract. A copy of this contract that was filed with TDCI by Universal is attached hereto as Exhibit B and incorporated herein by this reference. In light of this management contract, it appears that any liquidation of Universal cannot be carried out without the full cooperation of UCHS, its agents, employees, officers and directors. Accordingly, UCHS is named and served as a party Respondent herein so as to assist in obtaining its full cooperation.

IV. FACTUAL ALLEGATIONS

8. Respondent Universal is a for-profit corporation licensed by TDCI to operate as HMO in the State of Tennessee. Beginning in July 1, 2001, Universal contracted with the TennCare Bureau, pursuant to the CRA to act as an MCO to provide or arrange for health care

services to be provided to certain eligible enrollees in Tennessee's TennCare Program. Universal chose a full risk plan and did not take any risk sharing options offered by the State.

9. Effective April 12, 2002, the State and Universal entered into an amendment to the CRA (Amendment No. 2), which placed Universal on a no-risk basis. In general, this contract change meant that the State paid Universal an administrative fee and Universal was reimbursed for invoices for premium tax and medical services provided post-April 11, 2002.

10. As a TennCare MCO, Universal became subject to the regulatory provisions of chapter 32 of Title 56 of the Insurance Code. Tenn. Code Ann. § 56-32-212(a) expressly provides that "[t]o ensure the public's interest in the delivery of health care services by fiscally sound [HMOs]" each HMO must provide the Commissioner evidence of compliance with the minimum net worth requirements established in that statute. Pursuant to Tenn. Code Ann. § 56-32-212, Universal was required to maintain a minimum net worth of \$7,667,834 as of December 31, 2002. See Affidavit of John Mattingly, TDCI, TennCare Examinations Director, attached hereto as Exhibit C and incorporated herein by this reference.

11. **Net worth** is defined as meaning the excess of total *admitted assets* over total *admitted liabilities*, but the liabilities cannot include fully subordinated debt approved by the Commissioner. As used in statutory accounting practice, the term "admitted assets" is a standard, which by law, and by reference to the National Association of Insurance Commissioners ("NAIC") accounting practices, limits the types of assets regarded as sufficiently liquid and certain to be received by an HMO to be applied against its liabilities so as to be available to pay the costs of providing health care services to enrollees. Tenn. Code Ann. § 56-

32-212(a)(5) provides that for purposes of calculating a health maintenance organization's net worth, "admitted assets" include the following:

- (A) Petty cash and other cash funds in the organization's principal or official branch office that are under the organization's control;
- (B) Immediately withdrawable funds on deposit in demand accounts, in a bank or trust company organized and regularly examined under the laws of the United States or any state, and insured by an agency of the United States government, or like funds actually in the principal or official branch office at statement date and in transit to a bank or trust company with authentic deposit credit given before the close of business on the fifth bank working day following the statement date;
- (C) The amount fairly estimated as recoverable on cash deposited in a closed bank or trust company, if the assets qualified under this section before the suspension of the bank or trust company;
- (D) Receivables due from persons that are not more than ninety (90) days past due;
- (E) Amounts due under reinsurance arrangements from insurance companies authorized to do business in this state;
- (F) ***Undisputed*** tax refunds or other receivables due from the United States or this state;
- (G) Amounts on deposit under subsection (b); and
- (H) Investments determined as allowable by the commissioner under § 56-32-211.

(Emphasis added). Thus, assets can be "non-admitted" for statutory (HMO-regulatory) accounting purposes even though they might be "admitted" in the context of generally accepted accounting principles (GAAP) to be included and counted in a company's balance sheet. *Id.*

12. On March 26, 2002, the TennCare Bureau sent a letter to Universal notifying Universal that pursuant to Section 4-2.b. of the Contractor Risk Agreement ("CRA"), it was terminating the CRA, effective as of April 30, 2002, based upon the following breaches:

- a. (i) Failure to demonstrate sufficient financial capital to ensure uninterrupted delivery of health care on an ongoing basis in accordance with Title 56, Chapter 32, Part 2 or Universal's certificate of authority requirements as required by § 2-2.e. of the CRA; and

(ii) Failure to demonstrate evidence of compliance in the financial reports filed with the Tennessee Department of Commerce and Insurance, (“TDCI”), TennCare Division, that reflect that Universal has maintained the minimum net worth requirements and financial reserves required by TDCI of health maintenance organizations licensed by the State of Tennessee, including but not limited to the reserves required by Tenn. Code Ann. § 56-32-212 as amended [and] as required by § 2-9.3 of the CRA.

b. Failure to have and maintain a properly working claims processing system as required by §§ 2-9.g. and 2-18.w. of the CRA and also Tenn. Code Ann. § 56-36-226.

The letter further stated that TennCare was terminating the CRA for cause for breach of Section 4-2.d. of the CRA,

based upon TennCare’s reasonable determination that Universal’s financial condition is not sufficient to allow Universal to provide the services as described in the CRA required by TennCare because Universal cannot demonstrate (and has not demonstrated) to TennCare’s satisfaction that Universal has risk reserves and a minimum net worth sufficient to meet the statutory standards for licensed health maintenance organizations.

A copy of this March 26, 2002 letter of termination is attached hereto as Exhibit D and incorporated herein by this reference.

13. In addition to terminating the CRA for cause as a result of the identified breaches of the CRA, TennCare also notified Universal in the March 26th letter that it was terminating the CRA for convenience, pursuant to Section 4-2.e. of the CRA. That section provides that “TENNCARE may terminate this Agreement for convenience and without cause upon thirty (30) days written notice. Said termination shall not be a breach of contract by TENNCARE and

TENNCARE shall not be responsible to the CONTRACTOR or any other party for any costs, expenses, or damages occasioned by said termination, i.e., without penalty.” *Id.*

14. Thereafter, in May 2002, Universal and the State discussed the terms and conditions of a proposed Settlement and Release Agreement, which provided that upon execution of the proposed Agreement and subject to the full approval of the federal Centers for Medicaid and Medicare Services (“CMS”), the State of Tennessee, through the TennCare Bureau, would remit funds in an amount equal to approximately 90% of its pre-April 12, 2002, debt, but in no event in excess of \$61 million, to Universal, to be placed in a separate interest-bearing account for the purposes of retiring the debt of Universal to providers for health and medical care services rendered to enrollees from July 1, 2001, to April 11, 2002. The use of such funds for the payment of this debt was to be done in full accordance with the terms of an Agreed Order of Supervision, wherein TDCI would have to preapprove any disbursements of funds. A copy of this proposed Settlement and Release Agreement is attached hereto as Exhibit E and incorporated herein by this reference. This proposed Settlement and Release Agreement has not been fully approved by CMS, or by any of the state officials required by Tenn. Code Ann. § 20-13-103.

15. Because the proposed Settlement and Release Agreement was specifically conditioned upon CMS approval and such approval was not immediately forthcoming, the TennCare Bureau extended the effective date of termination on a weekly basis. Specifically, the TennCare Bureau sent a letter to Universal each Monday stating that TennCare was extending the effective date of termination until 11:59 p.m. CDST the following Monday “[b]ecause the Settlement Agreement is contingent upon approval by the Centers for Medicare and Medicaid

Services (“CMS”).” *See* Affidavit of Betty Boner attached hereto as Exhibit F and incorporated herein by this reference. After CMS did not approve the proposed Settlement and Release agreement, including the payment of the matching federal share of the \$61 million payment to Universal the State required to participate in the proposed Agreement, TennCare’s last weekly letter did not extend the effective date of termination beyond March 24, 2003. *Id.*

16. On September 13, 2002, Universal entered an Agreed Notice of Administrative Supervision with TDCI. A copy of the Agreed Notice of Administrative Supervision is attached hereto as Exhibit G and incorporated herein by this reference. The Agreed Notice of Administrative Supervision required that all medical and administrative disbursements be reviewed and pre-approved by TDCI, and further provided, in part, that:

A separate bank account must be established for any funds received from the State for payment of services prior to the non risk agreement. Any funds received by Universal for payment of services prior to the non risk period must be utilized by Universal to retire the debt. A plan must be submitted by the Supervisor prior to such debt being retired.

By its terms, this Agreed Notice of Administrative Supervision expired November 13, 2002, however the parties continued to treat it as being in effect. *See* Affidavit of John Mattingly, Exhibit C.

17. On December 31, 2002, Universal entered into a second Agreed Notice of Administrative Supervision with TDCI, containing similar terms as set forth above. A copy of this Agreed Notice of Administrative Supervision is attached hereto as Exhibit H and incorporated herein by this reference. Pursuant to its terms, this Administrative Supervision remains in effect until June 30, 2003, unless otherwise extended.

18. On March 1, 2003, Universal filed its NAIC Annual Statement with TDCI for the year ending December 31, 2002. This Annual Statement reported that Universal had a net worth, as of December 31, 2002, of \$6,809,449.00, ***resulting in a statutory net worth deficiency of \$858,385.00 (prior to any adjustments by TDCI for inaccurate reporting).***¹ A copy of this Annual Statement is attached hereto as Exhibit I and incorporated herein by this reference.

19. Adjustments by TDCI for inaccurate reporting on this Annual Statement reduced Universal's net worth to a negative \$2,784,325, thus giving Universal an adjusted statutory net worth deficiency of approximately \$10,452,159. *See* Affidavit of John Mattingly, Exhibit C.

20. Additionally, this Annual Statement listed as an admitted asset \$44,723,508 in "accident and health care premiums due and unpaid." as a receivable allegedly due from the TennCare Bureau.² These are disputed receivables and, therefore, cannot, as a matter of law, qualify as admitted assets pursuant to Tenn. Code Ann. § 56-32-212(a)(5)(F), which provides that only "***undisputed*** . . . receivables due from the United States or this state" may be considered an admitted asset for net worth purposes. Without these disputed receivables, Universal's net worth

¹Universal's statutory net worth requirement, as of December 31, 2002, was \$7,667,834. *See* ¶ 10, *supra*.

²This alleged receivable is for payments Universal claims the State owes it under the CRA to satisfy pre-April 12, 2002, debt to providers. From an analysis of Universal's claims data file representing all unpaid claims for dates of service before April 12, 2002, TDCI calculates that Universal's pre-April 12, 2002, debt (provider claims unpaid) is \$59,426,102. Additionally, it should be noted that this figure excludes \$683,029 in receivables reported from the State which Universal admits have in fact already been collected. *See* Affidavit of John Mattingly, Exhibit C.

is further reduced to a ***negative \$47,507,833***, resulting in a ***statutory net worth deficiency of \$55,175,667***, as of December 31, 2002.³ *Id.*

³On April 3, 2003, Universal filed its first amended 2002 NAIC Annual Statement with TDCI in which this receivable allegedly due from the State increased, without explanation, from \$44,723,508 to \$54,436,971. Thereafter, on May 7, 2003, Universal filed a second amended 2002 NAIC Annual Statement with TDCI in which it adjusted its total capital and surplus so that reported total admitted assets agreed with the reported total liabilities and capital surplus. This statement continued to report the \$54,436,971 receivable allegedly due from the State. Universal also reported \$1,524,942 as a receivable due from TennCare for preventive care services. This receivable has not been approved by TennCare and, thus, is a disputed receivable pursuant to Tenn. Code Ann. § 56-32-212(a)(5)(F). Accordingly, based on Universal's second amended 2002 NAIC Annual Statement, TDCI has calculated Universal's adjusted net worth as negative \$46,900,991, resulting in a statutory net worth deficiency of \$54,568,825, as of December 31, 2002. *See* Affidavit of John Mattingly, Exhibit C. Additionally, On June 3, 2003, Universal submitted its First Quarter 2003 NAIC Statement to TDCI. This statement shows that Universal continues to remain significantly insolvent. Universal's reported net worth of \$6,451,709 as of March 31, 2003, results in a ***statutory net worth deficiency of \$1,216,125 prior to any adjustments by TDCI for inaccurate reporting***. Universal continues to report the alleged receivables of \$54,436,971 due from the TennCare Bureau. Adjustments for the disputed receivables causes Universal's ***net worth to be reduced to a negative \$47,985,262, resulting in a***

net statutory net worth deficiency of \$55,653,096 as of March 31, 2003. Id.

21. On April 2, 2003, the State delivered a letter to Universal, in which it gave second written notice to Universal that its CRA with the State of Tennessee *d/b/a* TennCare Bureau was terminated effective June 1, 2003. The letter set forth the reasons for termination, which included the reasons set forth in the March 26, 2002, notice of termination; termination for convenience, as well as for cause; and, CMS's refusal to fully approve the proposed Settlement Agreement (including funding the proposed payment to Universal), as well as the fact that appropriate state officials had not approved the proposed Settlement. A copy of this April 2, 2003, Letter of Termination is attached hereto as Exhibit J and incorporated herein by this reference.

22. As previously noted, virtually 100% of Universal's revenue was from the payments from the State under the CRA, which has been terminated and such termination became effective on June 1, 2003. There is not any identifiable source of revenue or capital infusion to correct Universal's overwhelming net worth deficiencies within a reasonable time, and Universal's shareholders and management have advised TDCI that no more capital will be infused into the company. Additionally, at least two providers (or provider groups) have obtained judgments totaling several million dollars against Universal for unpaid claims for services rendered prior to April 11, 2002, and it is believed that more lawsuits by providers against Universal are pending. *See* Affidavit of John Mattingly, Exhibit C.

V. THE LAW

23. Tenn. Code Ann. § 56-9-306, under "FORMAL PROCEEDINGS" in the Rehabilitation and Liquidation Act, authorizes the Commissioner to apply by petition to the

Davidson County Chancery Court for an Order authorizing her to liquidate a domestic insurance company. Health maintenance organizations, such as Universal, are deemed to be “insurers” for purposes of applying the Act. *See* Tenn. Code Ann. § 56-9-103(12) and § 56-9-102(7). A liquidation proceeding may be based upon one or more of the grounds stated in Tenn. Code Ann. § 56-9-301 or 306, including that:

- (1) **The insurer is insolvent; or**
- (2) **The insurer is in such condition that further transaction of business would be hazardous financially to its policyholders, creditors or the public.**

“Insolvency” is defined under the Act as when an insurer is “unable to pay its obligations when they are due, or *when its admitted assets do not exceed its liabilities*, plus the greater of: (i) Any capital and surplus required by law for its organization; or (ii) the total par or stated value of its authorized and issued capital stock.” Tenn. Code Ann. § 56-9-103(11)(B)(emphasis added).

24. Similarly, the HMO statute specifically permits the Commissioner to apply for an order directing the Commissioner to rehabilitate, liquidate, conserve or supervise a health maintenance organization under the Act for any ground set out in title 56, chapter 9, or, when, in the Commissioner’s opinion, the continued operation of the health maintenance organization would be hazardous either to the enrollees or to the people of this state. Tenn. Code Ann. § 56-32-217(a). In the case of a net worth deficiency of an HMO, Tenn. Code Ann. § 56-32-212(a)(7) specifically permits the Commissioner to take action against the HMO under Tenn. Code Ann. § 56-32-217 if:

- (A) A health maintenance organization does not propose a plan to correct its working capital or net worth deficiency within the time frame described above;

(B) A health maintenance organization violates a plan that has been approved;

(C) The commissioner determines that ***an improper working capital or net worth status cannot be corrected within a reasonable time***; or

(D) The commissioner determines that ***an organization is in such financial condition that the transaction of further business would be hazardous to its enrollees, its creditors, or the public***. (Emphasis added).

25. The Uniform Insurers Rehabilitation and Liquidation Act does not require the Commissioner to petition for rehabilitation before seeking liquidation. Rather, the Act authorizes the Commissioner to petition to liquidate a domestic insurer, including Universal, “whether or not there has been a prior order directing the rehabilitation of the insurer.” Tenn. Code Ann. § 56-9-306(1).

26. Moreover, the grounds for liquidation do not require the Commissioner to prove that an HMO is insolvent, or to wait for that degree of financial crisis before taking action for the protection of enrollees, providers and other creditors. A hazardous condition ***short of insolvency*** is a ground for liquidation, consistent with the purposes of the Act, as set forth in Tenn. Code Ann. § 56-9-101(d), including “[e]arly detection of any potentially dangerous condition in an insurer, and prompt application of appropriate corrective measures.” Thus, there is no requirement that the Commissioner wait until insolvency strikes or the HMO actually stops meeting its debts and contractual obligations before she is empowered to act if she detects a prospective financial hazard to enrollees, providers and other creditors. However, as demonstrated by its own financial statements, Universal is clearly insolvent as that term is defined

in the Act and in accordance with statutory accounting principles, i.e., *Universal's total admitted assets do not exceed its total admitted liabilities.*

27. Moreover, as discussed *supra*, the State has terminated the Contractor Risk Agreement with Universal, which accounted for 100% of Universal's revenue. Based on the foregoing, it does not appear that Universal's statutory net worth deficiency can be corrected in a reasonable time so that the further transaction of Universal's business would not be hazardous to its enrollees, creditors and the public.⁴ Accordingly, the Commissioner has determined that Universal is insolvent and/or in a hazardous financial condition and, therefore, the grounds for liquidation are present here.

28. Pursuant to Tenn. Code Ann. § 56-9-133, this Verified Petition and exhibits filed thereto shall be received as prima facie evidence of the facts contained herein.

VI. FEATURES OF LIQUIDATION RECEIVERSHIP

29. **Management and Possession of Universal.** When a liquidator is appointed pursuant to Tenn. Code Ann. § 56-9-306, several statutory powers flow from the order of liquidation. The order to liquidate the HMO directs the Commissioner, as Liquidator,

⁴As discussed further herein, on May 30, 2003, Universal filed a claim with the Tennessee Claims Commission against the State, seeking \$75 million dollars in damages for alleged breach of the CRA by the State. This claim cannot provide any basis for correcting Universal's net worth deficiency, as the outcome of the proceeding before the Claims Commission is in dispute and purely speculative. Furthermore, it will be some time before the claim is fully resolved.

immediately to take possession of the assets of Universal, and vests title to all assets in the Liquidator. Tenn. Code Ann. § 56-9-307(a). Upon issuance of the order to liquidate, the rights and liabilities of any such insurer, its creditors, policyholders, shareholders and members and all other persons interested in its estate shall become fixed as of the date of entry of the order. Tenn. Code Ann. § 56-9-307(b).

30. **Injunctive Relief.** The Commissioner, as Liquidator, has the ability to apply for restraining orders, temporary and permanent injunctions under Tenn. Code Ann. § 56-9-105 to prevent transaction of the insurer's business, transfer of property, interference, waste of assets, destruction of records or data, or continuation or initiation of a number of types of actions against the insurer or its policyholders or enrollees. The Commissioner requests such injunctions against the institution of any action against Universal for the protection of Universal and its former enrollees, as well as its providers and creditors, upon the appointment of a receiver, all as more fully set forth in the Order terms in the prayer for relief hereto. Additionally, Tenn. Code Ann. § 56-9-313 provides that, upon issuance of an order appointing a liquidator of a domestic insurer,

no action at law or equity or in arbitration shall be brought against the insurer or liquidator, whether in this state or elsewhere, nor shall any such existing actions be maintained or further presented after issuance of such order.

Finally, under Tenn. Code Ann. § 56-9-106, all persons who have been performing or are concerned in any way with the affairs of Universal are required to cooperate with the Liquidator.

31. **Avoidance Powers.** The filing of a petition for liquidation affords statutory remedies upon the entry of an order of liquidation that enable the Liquidator to avoid preferential, fraudulent and certain other financial transfers prior to the filing date of the petition. These

statutory powers, found at Tenn. Code Ann. §§ 56-9-315, 316 and 317, are desirable because they increase the possible available funds for the benefit of the liquidating insurer's policyholders and creditors. There are additional recovery provisions granted to the Liquidator under Tenn. Code Ann. § 56-11-213 relating to the parent and affiliates of the HMO.

32. **Maintenance of Legal Actions.** On May 30, 2003, Universal filed a claim against the State of Tennessee, Department of Finance and Administration; M. D. Goetz, Jr., in his official capacity as Commissioner of the Department of Finance and Administration; and, Manny Martins, in his official capacity as Director of the TennCare Bureau, in the Claims Commission, alleging that the State had breached its TennCare contract with Universal and seeking to recover damages in the amount of \$75 million. The State has not yet had the opportunity to answer, and this case is still pending. However, as set forth in the April 2, 2003, Termination Letter, TennCare disputes this alleged receivable (or debt). On April 11, 2003, Universal filed a lawsuit in the United States District Court, Middle District of Tennessee, against Commissioner Goetz and Manny Martins in their official capacities, seeking to enjoin termination of the CRA prior to a pre-termination hearing (*Universal Care of Tennessee, Inc. v. M.D. Goetz, Jr., et al.*, No. 3-03-0324). Universal's application for a preliminary injunction was denied by the federal court in a memorandum and order issued May 30, 2003 (a copy of which is attached hereto). The State has moved to dismiss the lawsuit and thus, the case is still pending.

The Liquidator has the power to "continue to prosecute and institute in the name of the insurer, or in the liquidator's own name, any and all suits and other legal proceedings, in this state or elsewhere, and abandon the prosecution of claims the liquidator deems unprofitable to pursue further." Tenn. Code Ann. § 56-9-310(a)(14). As such, the Liquidator will be required to

evaluate the above-referenced lawsuits on behalf of the estate of Universal. Accordingly, the Commissioner has retained the services of William B. Hubbard, Esq., of the firm of Weed, Hubbard, Berry & Doughty, as special counsel to advise and assist her as Liquidator in the evaluation of these lawsuits, in accordance with her statutory duty.

33. Additionally, the deposit made by Universal under Tenn. Code Ann. § 56-32-212(b) with the Commissioner vests in the State immediately prior to the filing of this Petition. Although HMO enrollees in Tennessee do not have access to a guaranty fund, the special deposit serves some of the same purposes. Tenn. Code Ann. § 56-32-212(b)(7) states that the deposit shall be used and shall be considered held in trust to protect the interests of the HMO's enrollees and to assure continuation of health care services to enrollees of a HMO that is in rehabilitation or liquidation. The order of liquidation prayed for below provides that the deposit funds be made available to the liquidator to serve the purposes of the statute.

34. As discussed previously, effective April 12, 2002, Universal entered into an amendment to the CRA (Amendment No. 2), which placed Universal on a no-risk basis. In general, this contract change meant that the State paid Universal an administrative fee and Universal was reimbursed for invoices for premium tax and medical services provided post-April 11, 2002.⁵ With this amendment in place, Universal incurred no further debt with respect to its providers and was able to continue operations until the CRA terminated June 1, 2003.

⁵This no-risk aspect of the CRA was incorporated into Amendment No. 4 to the CRA, which extended the term of the CRA from July 1, 2002 to December 31, 2003. Copies of Amendments No. 2 and 4 are attached hereto as Collective Exhibit J and incorporated herein by this reference.

35. In addition, while Universal ceased to provide access to medical services to TennCare enrollees at midnight, May 31, 2003, the Commissioner, as Liquidator, anticipates that Universal will continue to receive bills, invoices and/or claims from providers for covered services incurred by TennCare enrollees during the period of April 12, 2002, through May 31, 2003 (the “run-off claims”). The Commissioner, as Liquidator, anticipates that Universal will continue to receive sufficient funds from TennCare to pay providers for these “run-off claims.”

VII. CONCLUSION

36. For all the foregoing reasons, the Commissioner submits that circumstances support entry of an order of liquidation. Furthermore, the Commissioner submits that Universal should be required to respond promptly to this Petition, and that a hearing on this Petition should be granted promptly because of the Commissioner’s immediate need for the statutory powers of a Receiver.

WHEREFORE, premises considered, Petitioner prays as follows:

A. That an Order Appointing the Commissioner and her successors in office as Liquidator of Respondent Universal Care of Tennessee, Inc., (“Universal”) be entered with substantially the following terms:

1. The Commissioner of Commerce and Insurance for the State of Tennessee, Paula A. Flowers (“Commissioner”), in her official capacity or her successors in office, is appointed Liquidator of **Universal Care of Tennessee, Inc.**, a Tennessee domiciled health maintenance organization ("Universal", Respondent" or "insurer") for purposes of liquidation as provided by Tenn. Code Ann. §§ 56-9-306, and 307 with all the powers conferred by law on receivers and liquidators of insurers appointed under those statutes. In addition to those powers specifically enumerated in this Final Order of Liquidation and by operation of law

under Tenn. Code Ann. §§ 56-9-101 *et seq.* for liquidators of insurers, the Liquidator shall have the power to exercise all powers now held or hereafter conferred upon receivers by the laws of this state not inconsistent with Tenn. Code Ann. §§ 56-9-101, *et seq.*;

2. Pursuant to Tenn. Code Ann. § 56-9-307, the Commissioner, as Liquidator, is authorized and directed forthwith (1) to take possession of all accounts, assets, monies, and property (both tangible and intangible) belonging to, held by and/or in the name of Universal Care of Tennessee, both within and without the State of Tennessee, (2) to be vested by operation of law with the title to all of the property, contracts and rights of action, and all of the accounts, assets, monies, books and records of the insurer, wherever located, as of the date of entry of the liquidation order, and any further title or rights in property gained by the Commissioner by virtue of such receivership, and (3) to have the right to recover the same and reduce the same to possession and to administer them under the general supervision of the Court with all the powers granted a Liquidator and receivers under Tenn. Code Ann. §§ 56-9-101 *et seq.* The Commissioner shall have immediate access to and shall occupy and control the premises and all records, databases, and computer files used to carry out the business of Universal, regardless of their location and possession;

3. Any bank, savings and loan association, financial institution or other person, which has on deposit, in its possession, custody or control any funds, accounts and any other assets of Universal Care of Tennessee, including financial institution accounts held in the name of other account holders, shall immediately transfer title, custody and control of all such funds, accounts, or assets to the Liquidator, and are hereby instructed that the Liquidator has absolute control over such funds, accounts and other assets. The Liquidator may change the name of such accounts and other assets, withdraw them from such bank, savings and loan association or other financial institution, or take any lesser action necessary for the proper conduct of this receivership. No bank, savings and loan association or other financial institution shall exercise any form of set-off, alleged set-off, lien, any form of self-help whatsoever, or refuse to transfer any funds or assets to the Liquidator's control without the permission of this Court;

4. Any entity (including any affiliate of Universal), including but not limited to Universal Care, Inc. (UCI) and Universal Care Health Systems (UCHS), which has custody, control or possession of any data processing information and records (including but not limited to source documents, all types of electronically stored information, master tapes, hard drives or any other record information) relating to or pertaining to Universal, shall make immediately available to the Commissioner as Liquidator for review and inspection of all such records in a form readable and/or accessible by the Commissioner, as of the date of this Order, unless

instructed to the contrary by the Commissioner as Liquidator. The Commissioner is authorized to make the determination as to which records, in the custody, control and possession of any entity other than Universal, relate to or pertain to Universal. If a dispute arises as to which records relate to or pertain to Universal, the entity shall file a motion with this Court for a hearing to resolve the dispute.

5. Pursuant to Tenn. Code Ann. § 56-9-307, the rights and liabilities of Universal and of its creditors, policyholders, shareholders, members and all other persons interested in its estate shall become fixed as of the date of the entry of this Order of Liquidation, except as provided in Tenn. Code Ann. §§ 56-9-308 and 326;

6. Pursuant to Tenn. Code Ann. § 56-9-308, all policies, including bonds and other noncancellable business, in effect at the time of issuance of this Order of Liquidation shall continue in force only for the lesser of: (1) a period of thirty (30) days after the date of entry of the Order of Liquidation, (2) the expiration of the policy coverage; (3) the date when the insured has replaced the insurance coverage with equivalent insurance in another insurer or otherwise terminated the policy, (4) the date when the liquidator has effected a transfer of the policy obligation pursuant to Tenn. Code Ann. § 56-9-310(a)(10), or, (5) the date proposed by the liquidator and approved by the Court to cancel coverage. The Liquidator proposes and the Court hereby approves that all outstanding policies and coverage be canceled on _____, 2003 [31st day after date of entry of this Order] at 12:01 a.m.;

7. This Order of Liquidation shall terminate coverage at the time specified in Tenn. Code Ann. § 56-9-308(a) for purposes of any other statute;

8. The Liquidator shall have all the powers enumerated in Tenn. Code Ann. § 56-9-310, including the power to appoint a special deputy or deputies to act for her and to determine their reasonable compensation. One such special deputy to be appointed by the Commissioner for purposes of liquidation is ***Paul Eggers***. The special deputy shall have all powers of the Liquidator as granted by this Order and as enumerated in Tenn. Code Ann. § 56-9-310. The special deputy shall serve at the pleasure of the Liquidator;

9. The Liquidator shall have the power to employ employees and agents, legal counsel, actuaries, accountants, appraisers, consultants and such other personnel as the Liquidator may deem necessary to assist in the liquidation, including, but not limited to, Universal Care, Inc. and Universal Care Health Systems, or any subcontractor thereof. If requested by the Liquidator, all legal counsel, actuaries, accountants, appraisers, consultants, subcontractors or vendors employed or retained by Universal, or performing services for or on behalf of Universal as of the date of this Order shall, within 30 days of such request, report

to the Liquidator the nature and status of the services they are handling or providing for or on behalf of Universal. Said report shall include an accounting of any funds received from or on behalf of Universal for any purposes and in any capacity as of the date of any such request from the Liquidator;

10. The Liquidator shall have the power to fix reasonable compensation of employees and agents, legal counsel, actuaries, accountants, appraisers and consultants with the approval of the Court, and shall have power to pay reasonable compensation to persons appointed and to defray from the funds or assets of the insurer all expenses of taking possession of, conserving, conducting, liquidating, disposing of, or otherwise dealing with the business and property of the insurer;

11. The Liquidator shall have the power to hold hearings, to subpoena witnesses to compel their attendance, to administer oaths, to examine any person under oath, and to compel any person to subscribe to his or her testimony after it has been correctly reduced to writing; and in connection therewith to require the production of any books, papers, records or other documents which he deems relevant to the inquiry;

12. The Liquidator shall have the power to audit the books and records of all agents of the insurer insofar as those records relate to the business activities of the insurer;

13. The Liquidator shall have the power to acquire, hypothecate, encumber, lease, improve, sell, transfer, abandon or otherwise dispose of or deal with, any property of the insurer at its market value or upon such terms and conditions as are fair and reasonable. The Liquidator shall also have power to execute, acknowledge and deliver any and all deeds, assignments, releases and other instruments necessary or proper to effectuate any sale of property or other transaction in connection with the liquidation;

14. The Liquidator shall have the power to enter into such contracts as are necessary to carry out the Order of Liquidation, and to affirm or disavow any contracts to which the insurer is a party;

15. The Liquidator shall have the power to continue to prosecute and to institute in the name of the insurer or in the Liquidator's own name any and all suits and other legal proceedings, in this state or elsewhere, and to abandon the prosecution of claims the Liquidator deems unprofitable to pursue further;

16. The Liquidator shall have the power to prosecute any action at law or in equity which may exist on the Liquidator's behalf, and/or on behalf of the

creditors, members, policyholders or shareholders of the insurer against any person or entity. Pursuant to Tenn. Code Ann. § 56-9-313(b)(1), the Liquidator may, within two (2) years or such other longer time as applicable law may permit, institute an action or proceeding on behalf of the estate of the insurer upon any cause of action against which the period of limitation fixed by applicable law has not expired at the time of the filing of the instant petition for liquidation;

17. Respondent Universal currently has pending two separate actions against the State of Tennessee: *Universal Care of Tennessee v. M. D. Goetz, Jr., et al.*, USDC No. 3-03-0324 and *Universal Care of Tennessee v. M.D. Goetz, Jr., et al.*, Tennessee Claims Commission No. _____. In light of the parties and allegations involved, and in order to properly perform the evaluation of whether to continue to prosecute or to abandon these suits against the State, the Commissioner has retained the services of William B. Hubbard, Esq., of the firm of Weed, Hubbard, Berry & Doughty, as special counsel to advise and assist her as Liquidator in the evaluation of these lawsuits, in accordance with her statutory authority as set forth in Tenn. Code Ann. § 56-9-310(a)(14).

18. The Liquidator shall have the power to remove any or all records and property of the insurer to the offices of the Commissioner or to such other place as may be convenient for the purposes of efficient and orderly execution of the liquidation;

19. The Liquidator shall have the power under Tenn. Code Ann. §§ 56-9-315, 316, and 317 to avoid fraudulent and preferential transfers and any applicable recovery powers authorized under Tenn. Code Ann. § 56-11-213;

20. The enumeration of the powers and authority of the Liquidator shall not be construed as a limitation upon the Commissioner or Special Deputy, nor shall it exclude in any manner any right to do such other acts not herein specifically enumerated or otherwise provided for, as may be necessary or appropriate for the accomplishment of or in aid of the purpose of liquidation;

21. The amounts held in the custodial deposit account established by Universal with the Commissioner under Tenn. Code Ann. § 56-32-212(b) to assure continuation of health care services to enrollees of Universal in rehabilitation or liquidation, which by operation of law vests in the State of Tennessee immediately prior to the filing of the petition for liquidation, shall be furnished by the State of Tennessee to the Liquidator for these purposes in the liquidation of Universal, for which the Liquidator may draw down such funds;

22. **Notice.** The Liquidator shall give or cause to be given notice of the Order of Liquidation in accordance with Tenn. Code Ann. § 56-9-311 as soon as

possible: (1) by first class mail and either by telegram or telephone to the insurance commissioner of each jurisdiction in which the insurer is doing business; (2) by first class mail to any guaranty association or foreign guaranty association which is or may become obligated as a result of liquidation; (3) by first class mail to all insurance agents of the insurer; (4) by first class mail to all persons known or reasonably expected to have claims against the insurer including all policyholders, at their last known address as indicated by the records of the insurer; and (5) by publication in a newspaper of general circulation in the county in which the insurer has its principal place of business and in such other locations as the liquidator deems appropriate;

23. **Claims Deadline** - Except as otherwise established by the Liquidator with approval of the Court, notice to potential claimants under Tenn. Code Ann. § 56-9-311(a) shall specify in the notice and require claimants to file with the Liquidator their claims together with proper proofs thereof under Tenn. Code Ann. § 56-9-324, on or before 4:30 p.m., Central Time, **January 15, 2004**, for purposes of participating in any distribution of assets that may be made on timely filed claims that are allowed in these proceedings;

24. With notice given in accordance with Tenn. Code Ann. § 56-9-311, the distribution of assets of the insurer under Tenn. Code Ann. §§ 56-9-101, *et seq.* shall be conclusive with respect to all claimants, whether or not they receive notice;

25. **Protection from Suit.** Pursuant to Tenn. Code Ann. § 56-9-313, no action at law or equity or in arbitration shall be brought against the insurer or Liquidator, whether in Tennessee or elsewhere, nor shall any such existing actions be maintained or further presented or prosecuted after issuance of the Order of Liquidation. All claims must be submitted through the claims process as set forth in the Act, and as further defined in this Order. Whenever, in the Liquidator's judgment, protection of the estate of the insurer necessitates intervention in an action against the insurer that is pending outside this state, the Liquidator may intervene in the action. The Liquidator may defend any action in which the Liquidator intervenes under this section at the expense of the estate of the insurer;

26. **Injunctions.** Pursuant to Tenn. Code Ann. § 56-9-105(a)(1-11), all persons, firms, corporations and associations, including, but not limited to, Respondent Universal Care of Tennessee, and its officers, directors, stockholders, members, subscribers, agents, attorneys, accountants, contractors, subcontractors, including, without prejudice to the generality, its management companies, Universal Care, Inc. and Universal Care Health Systems, their directors, agents, employees and officers, and any others, and all other persons with authority over or in charge of any segment of Universal's affairs, are prohibited and permanently

enjoined from (1) the transaction of Universal's business, (2) the waste or disposition of its property, (3) the destruction, deletion, modification, or waste of its records, databases or computer files, or any records databases or computer files relating to or pertaining to the business of Universal, regardless of the control, custody or possession of such records, (4) the commencement or prosecution of any actions, or the obtaining of preferences, judgments, attachments or other liens, or the making of any levy against the insurer or against its assets or any part thereof until further order of this Court, and (5) any other threatened or contemplated action, not permitted under the Act, that might lessen the value of the insurer's assets or prejudice the rights of policyholders, enrollees, creditors or shareholders, or the administration of any proceeding under the Act; and this Court further authorizes the Liquidator to apply outside of Tennessee for the relief described in Tenn. Code Ann. § 56-9-105(a);

27. **Cooperation.** Pursuant to Tenn. Code Ann. § 56-9-106, the officers, managers, directors, trustees, owners, employees, agents, attorneys, accountants, contractors or subcontractors of Universal, including, without prejudice to the generality, its management companies, Universal Care, Inc. and Universal Care Health Systems, their directors, agents, employees and officers, and any others, and any other persons with authority over or in charge of any segment of Universal's affairs, are ordered and required to cooperate with the Commissioner as Liquidator in the carrying out of the liquidation, including cooperating with the TennCare Bureau and the Commissioner as Liquidator in the orderly transfer of TennCare enrollees to another healthcare plan, as directed in the Amended and Restated Contrator Risk Agreement, specifically Sections 2-17 and 4-2. The term "person" shall include any person who exercises control directly or indirectly over activities of Universal through any holding company, parent company, or other affiliate of Universal. Further, the term "person" shall include any person who exercises control or who participates in the activities of the Universal, including through the record-keeping and computer systems operation relating to the activities of the Universal. "To cooperate" shall include, but shall not be limited to, the following: (1) to reply promptly in writing to any inquiry from the Commissioner requesting such a reply; and (2) to preserve and to make available to the Commissioner any and all books, bank and investment accounts, pension accounts, documents, or other records or information or computer programs and databases or property of or pertaining to Universal wheresoever located and in his or her possession, custody or control. No person shall obstruct or interfere with the Commissioner in the conduct of this liquidation;

28. Pursuant to Tenn. Code Ann. § 56-9-307(e), the Liquidator shall make financial reports to the Court, which shall be filed within one (1) year of the Order of Liquidation, and at least annually thereafter. Financial reports shall include the

assets and liabilities of the insurer and all funds received or disbursed by the Liquidator during the current period;

29. Any person, firm, corporation or other entity having notice of this Order that fails to abide by its terms shall be directed to appear before this Court to show good cause, if any they may have, as to why they should not be held in contempt of Court for violation of the provisions of this Order;

30. No bond is required of the Commissioner as a prerequisite for the filing of this petition or entry of this liquidation order or for the issuance of any injunction, restraining order, or additional order issued as provided by Tenn. Code Ann. § 20-13-101;

31. The Commissioner may apply to the Court for any further orders and injunctive relief which may be necessary to implement the terms of this order, or in aid thereof, to which the Commissioner may be entitled. This Court retains jurisdiction for the purpose of granting such further relief as from time to time shall be deemed appropriate, and;

32. That this Liquidation Order is permanent and a final order and entitled to full faith and credit, pursuant to U.S. Const. Art. IV, § 1 and 28 U.S.C. § 1738, in the state and federal courts of each of the United States.

33. That this Liquidation Order be posted on the Tennessee Department of Commerce and Insurance website.

B. That Universal be required to file a response to this Petition, that summons issue to all Respondents, and that an appropriate early hearing date be scheduled for this Petition;

C. That the filing of this Petition and any requested Order be entered without cost bond as provided by Tenn. Code Ann. § 20-13-101;

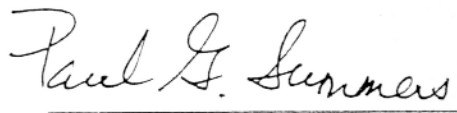
D. For such other relief as is appropriate.

THIS IS THE FIRST APPLICATION FOR THE EXTRAORDINARY RELIEF OF RECEIVERSHIP FOR THE PURPOSES OF LIQUIDATION.


Respectfully submitted,


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RECEIVERSHIP FOR THE PURPOSES OF LIQUIDATION.

Respectfully submitted,


PAUL G. SUMMERS (BPR 6285)
Attorney General and Reporter

(by *WEM*
with his
permission)


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IN THE CHANCERY COURT OF THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY

STATE OF TENNESSEE, ex rel.)
PAULA A. FLOWERS, Commissioner of)
Commerce and Insurance for the State)
of Tennessee,)
)
Petitioner,)
)
v.) No. _____
)
UNIVERSAL CARE OF TENNESSEE,)
INC., et al.,)
)
Respondents.)

VERIFICATION

STATE OF TENNESSEE)
COUNTY OF DAVIDSON)

1. I, Paula A. Flowers, am the duly appointed Commissioner of Commerce and Insurance for the State of Tennessee.

2. I have read the foregoing Verified Petition for Appointment of Receiver for Purposes of Liquidation and Injunction and swear that the information contained therein is true and correct to the best of my knowledge, information and belief.

Paula A. Flowers
PAULA A. FLOWERS
Commissioner of Commerce and Insurance
for the State of Tennessee

SWORN TO AND SUBSCRIBED before me on this 5th day of June,
2003.

Denise D. Beavis
NOTARY PUBLIC

My Commission Expires: My Commission Expires MAR. 27, 2004